Negotiable Instruments

Negotiable instruments are those documents which are used for making payments and whose ownership can be transferred from one person to another many times before the final payment is made. In other words, negotiable instrument is a transferable document, where negotiable means transferable and instrument means document. Moreover, a negotiable instrument means a document guaranteeing the payment of specific amount of money which is transferable from one person to another, either on demand or at some defined time, with the name of the payer on the instrument. According to section 13 of the Negotiable Instruments Act, 1881, a negotiable instrument can be defined as a “promissory note, bill of exchange, or cheque, payable either to order or to bearer”.

Further, the law related to negotiable instruments is enacted in India as Negotiable Instruments Act, 1881 and came into force from March 1, 1882 in the country. The Act is applicable in the entire country, except in the state of Jammu & Kashmir. This law is commercial in nature and aims to regulate the payment-related settlements of trade and commerce. The Act is governed by the Reserve Bank of India Act, 1934.

Features of Negotiable Instruments

- Easy Transferable- A negotiable instrument is can be transferred freely. Generally, when one person transfers any property to another, the person is required to make a transfer deed, get it registered, pay stamp duty, etc. However, such formalities are not neede to be met while transferring a negotiable instrument. The ownership is changed by mere delivery (when payable to the bearer) or even by valid endorsement and delivery (when payable to order).

- Absolute Title- Negotiability of these instruments accords absolute and good title on the transferee. In simple words, it means that a person who receives a negotiable instrument has a clear and undisputable title to the concerned instrument. However, the title of the receiver will be absolute, only if he has got the instrument in good faith and for a valid consideration. Besides, the receiver should have no knowledge of the previous holder having any defect in his title and such an individual is known as holder in due course.

- Written form- A negotiable instrument must be in written form.

- Unconditional Order- In the negotiable instruments, an unconditional order or promise for payment must be mentioned.

- Payment- The instrument should have considered payment of a certain sum of money only and nothing else. To say, one cannot make a promissory note on assets, securities, or goods, etc.
Certain Time of Payment- It means that the instrument must be payable at a certain time mentioned there in the respective instrument.

Payee must be certain- This shows that the individual in whose favor the instrument is made must be named or described with reasonable certainty. The payee as a person can be individual, body corporate, trade unions, even secretary, director or chairman of an institution. The payee may be more than one person.

Signature- A negotiable instrument must be signed by its maker. Without the signature of the drawer or the maker, the instrument shall be held invalid in the eyes of law.

Essence of Delivery- It is essential that the instrument must be delivered. Any negotiable instrument, such as, a cheque or a promissory note is incomplete till it is delivered to its payee.

Stamping- The stamping of Bills of Exchange and Promissory Notes is mandatory by law. The respective instrument must be duly stamped as per the Indian Stamp Act, 1899. Moreover, the value of stamp will depend upon the value of the promissory note or bill and the time of their payment.

Right to sue- The transferee of a negotiable instrument is entitled to file a suit in his own name for enforcing any right or claim on the basis of the instrument.

Transfer Notice- The notice of transfer of a negotiable instrument is not necessarily to be given to the party liable to pay the same.

Presumptions- There are some presumptions applicable to all negotiable instruments. To say, the consideration is presumed to have passed between the transferor and the transferee.

Transfer- The negotiable instruments can be transferred as and when required till they reached at their maturity.

Rule of evidence- The negotiable instruments are in written form and duly signed by the parties, and therefore, they can be used as evidence of the fact of indebtedness in the court of law because they have special rules of evidence.

Exchange- The negotiable instruments are concerned with the payment of certain money in legal tender, and hence they are regarded as substitutes for money and are accepted in exchange of goods because these are easily converted into cash by discounting and re-discounting.

Types of Negotiable Instruments

According to the Negotiable Instruments Act, 1881, the negotiable instruments include promissory note, bill of exchange and cheque only. However, some other documents are also recognized as negotiable instruments on the basis of custom and usage, like hundis, treasury bills, share warrants, etc., provided they are featured with negotiability.

Promissory Note
In the Negotiable Instruments Act (Section 4), 1881, a promissory note is defined as “an instrument in writing (not being a bank note or a currency note) contains an unconditional undertaking, signed by the maker, to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument”.

Specimen of a Promissory Note

<table>
<thead>
<tr>
<th>Rs. 10,000/-</th>
<th>New Delhi</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 25, 2020</td>
<td></td>
</tr>
</tbody>
</table>

On demand, I promise to pay Ram, s/o RamLal of Meerut or order a sum of Rs. 10,000/- (Rupees Ten Thousand only), for value received.

To, Ram

Address……..  Sd/ Shyam

Stamp

Parties to a Promissory Note

There are basically two parties involved in a promissory note:

1. The Maker or Drawer – the person who prepares the note and promises to pay the amount mentioned therein.
2. The Payee – the person to whom the amount is payable.

Features of a Promissory Note

- A promissory note should be in written form, duly signed by its maker or drawer and duly stamped as per the Indian Stamp Act.
- It must contain an undertaking or promise to pay the amount mentioned therein because only acknowledgement of indebtedness is not enough to serve the purpose.
- A promissory note must be containing an unconditional promise to pay.
- It must contain a consideration in monetary terms only.
- The parties involved in a promissory note must be certain.
- A promissory note should be payable either on demand or at a certain date.
- The sum payable mentioned there in the promissory note must be certain or capable of being made certain. It means that the sum payable may be in figures or may be such that it can be calculated.

Bill of Exchange

In the Negotiable Instruments Act (Section 5), 1881, a bill of exchange is defined as “an instrument in writing contains an unconditional order, signed by the maker, directs a certain person to pay a certain sum of money only to or to the order of a certain person, or to the bearer of the instrument”.
Specimen of a Bill of Exchange

<table>
<thead>
<tr>
<th>Rs. 20,000/-</th>
<th>New Delhi</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 25, 2020</td>
<td></td>
</tr>
</tbody>
</table>

Five months after date pay Shyam or (to his) order the sum of Rupees Twenty Thousand only for value received.

<table>
<thead>
<tr>
<th>To</th>
<th>Accepted</th>
<th>Stamp</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ram</td>
<td>Ram</td>
<td>S/d</td>
</tr>
<tr>
<td>Address</td>
<td>Shyam</td>
<td></td>
</tr>
</tbody>
</table>

Parties to a Bill of Exchange

There are basically three parties involved in a bill of exchange:

1. The Drawer – The person who makes the order for making payment.
2. The Drawee – The person to whom the order to pay is made.
3. The Payee – The person to whom the payment is to be made.

The drawer can also make a bill in his own name where he himself becomes the payee. In this case, the words in the bill would be Pay to us or order. In a bill of exchange where a time period is mentioned is called a Time Bill. However, a bill may be made payable on demand also which is called a Demand Bill.

Features of a bill of exchange

- A bill must be in written form, duly signed by its drawer, accepted by its drawee and duly stamped as per the Indian Stamp Act.
- A bill of exchange must be containing an unconditional order to pay.
- The unconditional order must be to pay in monetary terms only.
- The amount payable mentioned therein must be certain or capable of being made certain.
- The parties involved in a bill of exchange must be certain.

Cheque

In the Negotiable Instruments Act, 1881 a cheque is defined as a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand. Actually, a cheque is an order made by the account holder of the concerned bank directing his banker to pay on demand, the specified amount, to or to the order of the person named therein or to the bearer.
Specimen of Cheque

STATE BANK OF INDIA

Pay.................................................................

..............................................................or Bearer

Rupees.................................................Rs. ________

                  Signature

                  6 5 3 0 0 3            1 1 0 0 2 0 5 6

This is the basic format of cheque. However, it differs from bank to bank regarding their fonts, logo, MICR code and such other basic features of a cheque.

Features of a Cheque

- A cheque must be in written form and duly signed by the drawer.
- A cheque must contain an unconditional order.
- A cheque is issued on a specified banker only.
- The amount specified there in the cheque is always certain and must be clearly mentioned both in figures and words.
- The payee must be always certain.
- A cheque is payable on demand.
- The cheque must properly dated.

Types of Cheque

Open cheque:

An open cheque is the cheque which can be encashed over the counter at the bank. The holder of an open cheque can receive its payment over the counter at the bank, deposit the cheque in his own account or pass it to someone else by signing behind the cheque.

Crossed cheque:

Since an open cheque can be encashed by anyone whoever will present it at the counter of the bank, it is risky to issue such cheques and the risk can be mitigated by issuing another type of cheque called ‘Crossed cheque’. The payment of a crossed cheque is not made over the counter at the bank as it is only credited to the bank account of the payee mentioned therein the cheque. Moreover, a cheque can be crossed by drawing two transverse parallel lines across the cheque, with or without the writing ‘Account payee’ or ‘Not Negotiable’ and sometimes, bank’s name is also specified in between those two transverse parallel lines.
Bearer cheque:

A bearer cheque is such a type of cheque which is payable to any person who presents it for payment at the counter of the bank. It can be transferred by mere delivery and needs no endorsement.

Order cheque:

An order cheque is a cheque which is payable only to a particular person. In case of an order cheque, the word ‘bearer’ may be cut out or cancelled and the word ‘order’ may be written over there. The payee may transfer an order cheque to someone else by signing his or her name behind the cheque.

Ante-dated cheques:

A cheque in which the drawer mentions the date earlier to the date of presenting if for payment. For example, a cheque issued on March 20, 2020 may bear a date March 5, 2020.

Stale Cheque:

A stale cheque is the cheque which is issued at some particular date and must be presented before at bank for payment within a stipulated period as, no payment will be made after expiry of that period and the cheque will automatically stand cancelled.

Mutilated Cheque:

When a cheque is torn into two or more pieces or is in deteriorated condition and presented for payment, such a cheque is called a mutilated cheque. The bank has a right not to make payment against such a cheque without getting confirmation of the drawer. However, if a cheque is torn at the corners and no material fact is lost, the bank can initiate the payment against such a cheque.

Post-dated Cheque:

In case the drawer mentions a specific date on the cheque which is subsequent to the date on which it is presented, is called post-dated cheque. To say, if a cheque is presented on March 5, 2020 bears a date of March 25, 2020, it is considered a post-dated cheque by the bank and the payment can only be made on or after March 25, 2020.